

Auditing Procedures Report

Instructions and MuniCodes

*=Required Fields

Reset Form

Issued under Public Act 2 of 1968, as amended. (V1.07)

Unit Name* Kalkaska County Hospital Authority	County* KALKASKA	Type* AUTHORITY	MuniCode* 40 7501
Opinion Date-Use Calendar* Oct 4, 2008	Audit Submitted-Use Calendar* Oct 22, 2008	Fiscal Year End Month* 06	Fiscal Year* 2008

If a local unit of government (authorities & commissions included) is operating within the boundaries of the audited entity and is NOT included in this or any other audit report, nor do they obtain a stand-alone audit, enclose the name(s), address(es), and a description(s) of the authority and/or commission.

Place a check next to each "Yes" or non-applicable question below. Questions left unmarked should be those you wish to answer "No."

<input checked="" type="checkbox"/> ?	1. Are all required component units/funds/agencies of the local unit included in the financial statements and/or disclosed in the reporting entity notes to the financial statements?
<input checked="" type="checkbox"/> ?	2. Does the local unit have a positive fund balance in all of its unreserved fund balances/unrestricted net assets?
<input checked="" type="checkbox"/> ?	3. Were the local unit's actual expenditures within the amounts authorized in the budget?
<input checked="" type="checkbox"/> ?	4. Is this unit in compliance with the Uniform Chart of Accounts issued by the Department of Treasury?
<input checked="" type="checkbox"/> ?	5. Did the local unit adopt a budget for all required funds?
<input checked="" type="checkbox"/> ?	6. Was a public hearing on the budget held in accordance with State statute?
<input checked="" type="checkbox"/> ?	7. Is the local unit in compliance with the Revised Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, and other guidance as issued by the Local Audit and Finance Division?
<input checked="" type="checkbox"/> ?	8. Has the local unit distributed tax revenues, that were collected for another taxing unit, timely as required by the general property tax act?
<input checked="" type="checkbox"/> ?	9. Do all deposits/investments comply with statutory requirements including the adoption of an investment policy?
<input checked="" type="checkbox"/> ?	10. Is the local unit free of illegal or unauthorized expenditures that came to your attention as defined in the Bulletin for Audits of Local Units of Government in Michigan, as revised (see Appendix H of Bulletin.)
<input checked="" type="checkbox"/> ?	11. Is the unit free of any indications of fraud or illegal acts that came to your attention during the course of audit that have not been previously communicated to the Local Audit and Finance Division? (If there is such activity, please submit a separate report under separate cover.)
<input checked="" type="checkbox"/> ?	12. Is the local unit free of repeated reported deficiencies from previous years?
<input checked="" type="checkbox"/> ?	13. Is the audit opinion unqualified? 14. If not, what type of opinion is it? NA
<input checked="" type="checkbox"/> ?	15. Has the local unit complied with GASB 34 and other generally accepted accounting principles (GAAP)?
<input checked="" type="checkbox"/> ?	16. Has the board or council approved all disbursements prior to payment as required by charter or statute?
<input checked="" type="checkbox"/> ?	17. To your knowledge, were the bank reconciliations that were reviewed performed timely?
<input type="checkbox"/> ?	18. Are there reported deficiencies? 19. If so, was it attached to the audit report?

General Fund Revenue:	<input type="checkbox"/> ? \$ 21,471,074.00
General Fund Expenditure:	<input type="checkbox"/> ? \$ 20,242,373.00
Major Fund Deficit Amount:	\$ 0.00

General Fund Balance:	<input type="checkbox"/> ? \$ 22,460,485.00
Governmental Activities Long-Term Debt (see instructions):	<input type="checkbox"/> ? \$ 8,002,039.00

We affirm that we are certified public accountants (CPA) licensed to practice in Michigan. We further affirm the above responses have been disclosed in the financial statements, including the notes, or in the Management Letter (reported deviations).

CPA (First Name)* Randal	Last Name* Koning	Ten Digit License Number* OK CV		
CPA Street Address* 190 Carondelet Plaza	City* Saint Louis	State* MO	Zip Code* 63105	Telephone* +1 (314) 290-1000
CPA Firm Name* Ernst & Young LLP	Unit's Street Address* 419 S Coral	Unit's City* Kalkaska	Unit's Zip* 49646	

CONSOLIDATED FINANCIAL STATEMENTS

Kalkaska County Hospital Authority & Subsidiary
Years Ended June 30, 2008 and 2007
With Reports of Independent Auditors

Kalkaska County Hospital Authority & Subsidiary

Consolidated Financial Statements

Years Ended June 30, 2008 and 2007

Contents

Report of Independent Auditors	1
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Consolidated Financial Statements Performed in Accordance With <i>Government Auditing Standards</i>	3
Consolidated Financial Statements	
Consolidated Statements of Net Assets.....	5
Consolidated Statements of Revenues, Expenses, and Changes in Net Assets	6
Consolidated Statements of Cash Flows	7
Notes to Consolidated Financial Statements	8
Other Financial Information	
Details of Combining Statements of Revenue, Expenses, and Changes in Net Assets	22



Ernst & Young LLP
171 Monroe Avenue, NW
Grand Rapids, Michigan 49503

Tel: +1 616 774 0710
Fax: +1 616 774 0190
www.ey.com

Report of Independent Auditors

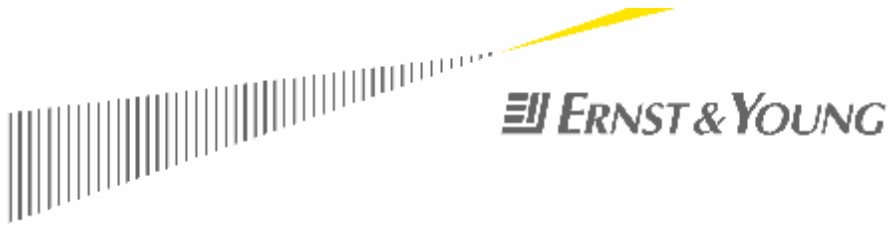
The Board of Directors
Kalkaska County Hospital Authority & Subsidiary

We have audited the accompanying consolidated statements of net assets of Kalkaska County Hospital Authority & Subsidiary (the Hospital) as of June 30, 2008 and 2007, and the related consolidated statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. We were not engaged to perform an audit of the Hospital's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Kalkaska County Hospital Authority & Subsidiary as of June 30, 2008 and 2007, and the changes in its net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States.

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The other financial information appearing on page 20 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.



In accordance with *Government Auditing Standards*, we have also issued our report dated October 4, 2008, on our consideration of Kalkaska County Hospital Authority & Subsidiary's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

The accompanying consolidated financial statements do not present management's discussion and analysis of the Hospital's financial position and operating results. The Governmental Accounting Standards Board has determined that this analysis is necessary to supplement, although not required to be part of, the basic consolidated financial statements.

Ernst & Young LLP

October 4, 2008



Ernst & Young LLP
171 Monroe Avenue, NW
Grand Rapids, Michigan 49503

Tel: +1 616 774 0710
Fax: +1 616 774 0190
www.ey.com

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Consolidated Financial Statements Performed in Accordance With *Government Auditing Standards*

The Board of Directors
Kalkaska County Hospital Authority & Subsidiary

We have audited the consolidated financial statements of Kalkaska County Hospital Authority & Subsidiary (the Hospital) as of and for the years ended June 30, 2008 and 2007, and have issued our report thereon dated October 4, 2008. We conducted our audits in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audits, we considered the Hospital's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.



Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Hospital's consolidated financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the board of directors, management, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

October 4, 2008

Kalkaska County Hospital Authority & Subsidiary

Consolidated Statements of Net Assets

	June 30	
	2008	2007
Assets		
Current assets:		
Cash and cash equivalents	\$ 5,507,453	\$ 3,343,367
Short-term investments	502,030	—
Accounts receivable	2,754,236	2,324,062
Third-party settlements	569,376	389,894
Prepaid expenses	388,951	259,419
Total current assets	9,722,046	6,316,742
Assets limited as to use	4,840,472	4,396,932
Property and equipment	21,855,671	12,504,542
Deferred charges	175,079	10,000
Total assets	<u>\$ 36,593,268</u>	<u>\$ 23,228,216</u>
Liabilities and net assets		
Current liabilities:		
Current maturities – long-term debt	\$ 740,552	\$ —
Trade accounts payable	3,742,307	1,115,468
Third-party settlements	—	354,800
Accrued liabilities and other	2,388,437	1,985,775
Total current liabilities	6,871,296	3,456,043
Long-term debt, less current maturities	7,261,487	—
Total liabilities	14,132,783	3,456,043
Net assets:		
Invested in capital assets, net of related debt	13,853,632	12,504,542
Unrestricted	8,606,853	7,267,631
Total net assets	22,460,485	19,772,173
Total liabilities and net assets	<u>\$ 36,593,268</u>	<u>\$ 23,228,216</u>

See accompanying notes.

Kalkaska County Hospital Authority & Subsidiary

Consolidated Statements of Revenues, Expenses, and Changes in Net Assets

	Year Ended June 30	
	2008	2007
Operating revenue		
Net patient service revenue	\$ 20,449,015	\$ 18,878,940
Other	1,022,059	850,321
Total operating revenue	21,471,074	19,729,261
Operating expenses		
Salaries and wages	8,472,821	7,849,827
Employee benefits and payroll taxes	2,750,128	2,703,584
Medical supplies and drugs	2,454,625	2,119,562
Professional services and consultant fees	523,512	478,374
Purchased services	2,579,191	2,179,471
Insurance	260,573	226,599
Occupancy	641,041	502,509
Equipment, software, and maintenance	358,413	399,078
Depreciation	1,132,128	1,154,652
Other	1,069,941	1,069,837
Total operating expenses	20,242,373	18,683,493
Operating income	1,228,701	1,045,768
Other income (expense)		
Investment income	212,158	186,998
Contributions	59,610	12,795
Interest on debt related to capital assets	(4,327)	(31,986)
Tax levy revenue	1,192,170	1,119,979
Total other income	1,459,611	1,287,786
Increase in net assets	2,688,312	2,333,554
Net assets at beginning of year	19,772,173	17,438,619
Net assets at end of year	\$ 22,460,485	\$ 19,772,173

See accompanying notes.

Kalkaska County Hospital Authority & Subsidiary

Consolidated Statements of Cash Flows

	Year Ended June 30	
	2008	2007
Operating activities		
Cash received from patients and third-party payors	\$ 19,484,559	\$ 18,625,125
Cash payments to suppliers for services and goods	(16,210,276)	(17,326,414)
Other receipts from operations	1,022,059	1,223,197
Net cash provided by operating activities	4,296,342	2,521,908
Noncapital financing activities		
Contributions	59,610	12,795
Investing activities		
Investment income	212,158	186,998
Net purchase of short-term investments	(502,030)	—
Net purchase of assets limited as to use	(443,540)	(1,121,191)
Net cash used in investing activities	(733,412)	(934,193)
Capital and related financing activities		
Acquisition and construction of capital assets	(10,255,091)	(1,545,937)
Proceeds from county tax levy	1,192,170	1,119,979
Interest paid on long-term debt	(232,493)	(31,986)
Issuance of long-term debt	8,400,000	—
Acquisition of Level Acres debt	102,039	—
Principal payments on notes payable	(500,000)	(750,000)
Net deferred charges	(165,079)	(5,271)
Net cash used in capital and related financing activities	(1,458,454)	(1,213,215)
Net increase in cash and cash equivalents	2,164,086	387,295
Cash and cash equivalents at beginning of year	3,343,367	2,956,072
Cash and cash equivalents at end of year	\$ 5,507,453	\$ 3,343,367
Reconciliation of operating income to net cash flows from operating activities		
Operating income	\$ 1,228,701	\$ 1,045,768
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	1,132,128	1,154,652
Provision for uncollectible accounts	983,157	753,037
(Increase) decrease in assets:		
Patient accounts receivable	(1,413,331)	(1,190,572)
Third-party settlements	(179,482)	401,220
Other current assets	(129,532)	68,104
Increase (decrease) in liabilities:		
Trade accounts payable	2,626,839	168,035
Third-party settlements	(354,800)	(217,500)
Other accrued liabilities	402,662	339,164
Net cash provided by operating activities	\$ 4,296,342	\$ 2,521,908

See accompanying notes.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements

Years Ended June 30, 2008 and 2007

1. Nature of Business and Significant Accounting Policies

Reporting Entity and Corporate Structure

Kalkaska County Hospital Authority & Subsidiary (the Hospital), d/b/a Kalkaska Memorial Health Center, is located in Kalkaska, Michigan, and provides inpatient, outpatient, and long-term care services primarily to the citizens of Kalkaska County, Michigan. The Hospital is organized as a governmental unit in accordance with the Joint Hospital Authority Act 47 of the Michigan Public Acts of 1984. Accordingly, the Hospital is not subject to income taxes, and no income tax provision has been recorded in the consolidated financial statements. The Hospital's consolidated financial statements are prepared on the accrual basis of accounting.

On December 6, 2007, Kalkaska County Hospital Authority became the sole member of Level Acres Non-Profit Housing Corporation, a Michigan non-profit corporation, and exempt under Section 501(c)(3) by the Internal Revenue Service. The transaction was accounted for as a contribution of \$59,587 (consisting of \$193,565 in assets and liabilities of \$133,978). The financial statements for 2008 include the financial activity for Level Acres Non-Profit Housing Corporation from December 6, 2007 through June 30, 2008. Also during the year the Hospital began providing dialysis services, which is approved by Medicare as a distinct unit.

Basis of Presentation

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles as prescribed by Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, issued in June 1999. The Hospital follows the "business-type" activities reporting requirements of GASB Statement No. 34, which provide a comprehensive look at the Hospital's financial activities. No component units are required to be reported in the Hospital's consolidated financial statements. The Hospital has elected not to apply provisions of relevant Financial Accounting Standard Board (FASB) statements.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from these estimates.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

1. Nature of Business and Significant Accounting Policies (continued)

Cash and Cash Equivalents

Cash and cash equivalents include cash and investments in highly liquid investments purchased with an original maturity of three months or less.

Short-Term Investments

Short-term investments include investments with an original maturity of greater than three months and less than one year.

Assets Limited as to Use

Assets limited as to use include assets designated by the Hospital's board to provide for future replacement of facilities and equipment.

Property and Equipment

Property and equipment are stated at cost. Depreciation is computed using straight-line methods over the estimated useful lives of the assets.

At June 30, 2008, the Hospital has building commitments totaling \$10.8 million. At June 30, 2007, the Hospital had building commitments totaling \$1.1 million.

Deferred Charges

Deferred charges represent legal, consulting, and financial costs associated with debt financing and are being amortized over the term of the debt agreement.

Classification of Net Assets

Net assets of the Hospital are classified into two components. Net assets invested in capital assets, net of related debt consist of capital assets net of accumulated depreciation reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets, net of related debt.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

1. Nature of Business and Significant Accounting Policies (continued)

Compensated Absences

Paid time off is charged to operations when earned. Unused and earned benefits are recorded as a current liability in the consolidated financial statements.

Revenue Recognition

Net patient service revenue is recognized at the time services are provided and is reported net of discounts and allowances (including provision for uncollectible accounts) of \$6,539,453 in 2008 and \$5,779,852 in 2007. The Hospital is designated as a critical access hospital under Medicare regulations. Under this designation, the Hospital receives 101% of reasonable, cost-based reimbursement for inpatient and outpatient services provided to Medicare beneficiaries.

Functional Classification of Expenses

The Hospital provides general healthcare services to resident within communities served, including inpatient, outpatient, and long-term care services. The Hospital does not report expense information by functional classification because its resources and activities are primarily related to providing healthcare services. Further, since the Hospital receives substantially all of its resources from providing healthcare services in a manner similar to a business enterprise, other indicators contained in these consolidated financial statements are considered important in evaluating how well management has discharged its stewardship responsibilities.

Operating Revenue and Expenses

The Hospital's consolidated statements of revenue, expenses, and changes in net assets distinguish between operating and nonoperating revenue and expenses. Operating revenue results from exchange transactions associated with providing health care services, the Hospital's principal activity. Nonexchange revenue, including taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenue. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

1. Nature of Business and Significant Accounting Policies (continued)

Charity Care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Gross charges for charity care for the years ended June 30, 2008 and 2007, were \$156,461 and \$86,629, respectively.

New Accounting Standards

During 2008, the Hospital adopted FASB Interpretation No. (FIN) 48, *Accounting for Uncertainty in Income Taxes – an Interpretation of (SFAS) No. 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. It also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 was effective for fiscal years beginning after December 15, 2006. The Hospital's adoption of FIN 48 had no material impact on the consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in accordance with accounting principles generally accepted in the United States, and expands disclosure about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. The Hospital has not determined the effect that the adoption of SFAS No. 157 will have on its consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. SFAS No. 159 permits companies to choose to measure certain financial instruments and other items at fair value that are not currently required to be measured at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Hospital has elected not to adopt SFAS No. 159.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

1. Nature of Business and Significant Accounting Policies (continued)

Reclassifications

During 2008, the Hospital installed new financial software and established a new chart of accounts. Due to this change, certain amounts previously reported in 2007 have been reclassified to conform with the presentation used in 2008. In management's opinion, the new chart of accounts better represents the Hospital's financial activities.

2. Cash and Investments

Michigan Compiled Laws Section 129.91 (Public Act 20 of 1943, as amended) authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The local unit is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United

States banks; commercial paper rated within the two highest classifications, which mature not more than 270 days after the date of purchase; obligations of the state of Michigan or its political subdivisions, which are rated as investment grade; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

The Hospital has designated four banks for the deposit of its funds. The Hospital's deposit policies are in accordance with statutory authority.

Due to the volatility of the stock market, there is a reasonable possibility of changes in fair value and additional investment gains and losses in the near term. The Hospital's cash and investments are subject to several types of risk, which are examined in more detail below:

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a bank failure, the Hospital's deposits and investments may not be returned to it. The Hospital does not have a deposit policy for custodial credit risk.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

2. Cash and Investments (continued)

At June 30, 2008 and 2007, the Hospital has \$5,193,941 and \$3,109,415, respectively, in cash and cash equivalents (certificates of deposit, short-term money market funds, checking accounts, and savings accounts) that is uninsured and uncollateralized. The Hospital believes that due to the dollar amounts of deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the Hospital evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

At June 30, 2008, the following investments (classified as assets limited as to use) are uninsured. Further, with the exception of the certificate of deposit at JPMorgan Chase in the amount of \$65,652 at June 30, 2008, these investments represent investments in any one issuer exceeding 5% of total investments.

Investment	Issuer	Fair Value
June 30, 2008		
Public funds money market	Huntington Bank	\$ 4,612,040
Certificates of deposit	JPMorgan Chase	\$ 65,652
June 30, 2007		
Certificates of deposit	Huntington Bank	\$ 2,619,854
Certificates of deposit	JPMorgan Chase	\$ 685,232

Interest Rate Risk

Interest rate risk is the risk that the value of investments will decrease as a result of a rise in interest rates. The Hospital's investment policy does not restrict investment maturities, other than commercial paper, which can only be purchased with a 270-day maturity. At year-end, debt investments are as follows:

Investment	Fair Value	Maturity Date	Call Option
June 30, 2008			
FHLB 4.27%	\$ 502,030	9/30/2008	Not callable
June 30, 2007			
FHLB 4.27%	\$ 494,065	9/30/2008	Not callable
FHLB 5.51%	\$ 499,220	4/26/2010	Quarterly

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

3. Accounts Receivable

The details of accounts receivable are set forth below:

	<u>2008</u>	<u>2007</u>
Accounts receivable	\$ 4,658,003	\$ 3,637,753
Less:		
Allowance for uncollectible accounts	382,954	239,909
Allowance for contractual adjustments	1,544,756	1,094,504
Net accounts receivable	<u>2,730,293</u>	<u>2,303,340</u>
Other	23,943	20,722
Total accounts receivable	<u>\$ 2,754,236</u>	<u>\$ 2,324,062</u>

The Hospital grants credit without collateral to patients, most of whom are local residents and are insured under third-party payor agreements. The composition of receivables from patients and third-party payors was as follows:

	<u>2008</u>	<u>2007</u>
Medicare	34%	37%
Blue Cross/Blue Shield of Michigan	17	18
Medicaid	27	24
Commercial insurance and HMOs	15	13
Self-pay	7	8
Total	<u>100%</u>	<u>100%</u>

4. Third-Party Settlements

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare and Medicaid programs. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

4. Third-Party Settlements (continued)

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactively calculated adjustments arising under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined. Net patient service revenue increased \$543,600 and \$472,203 for the periods June 30, 2008 and 2007, respectively, related to changes in estimated third-party settlements for prior years.

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. For 2008, approximately 87% (86% for 2007) of the Hospital's net patient service revenue is received from the Medicare, Medicaid, and Blue Cross Blue Shield of Michigan programs.

5. Tax Levies

The Hospital is operated under the Joint Hospital Authority Act 47 (the Act) of the Michigan Public Acts of 1984. Under the Act, by April 1 of each year, the Hospital board is required to prepare a balanced budget for the ensuing year. The budget is to ascertain what amount, if any, is to be raised by taxation from the townships belonging to the Authority to meet their respective shares of the expenses over revenue. Upon certification by the Hospital board, the townships are required to pay their share from the funds they have available or from the proceeds of a tax levy. They are authorized to levy up to .40 mil, but levied .01 mil for both the years ended June 30, 2008 and 2007. The required sums are due and payable 120 days after December 1, the date on which local taxes become due and payable in the townships.

In addition to the levy described above, the Act allows a levy up to 2 mils for not more than 10 years for capital improvements when approved at a general or special election in the townships belonging to the Authority.

In May 1997, the electorate approved a 1.7 mil levy for 10 years. The proceeds from the levy are to be used to retire unlimited tax general obligation bonds. The ordinance authorizing the sale of the bonds requires the proceeds of the 1.7 mil tax levy to be deposited in a bond and interest redemption fund. The amount in excess of the debt service payments must be deposited in a capital improvement fund and used for capital improvement purposes.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

5. Tax Levies (continued)

In May 2007, the electorate approved a 1.6 mil levy for 10 years, with the same terms and conditions as the previous levy.

Tax levy revenue is composed of the following:

	<u>2008</u>	<u>2007</u>
Operating tax levy	\$ 6,487	\$ 6,146
Bond retirement 1.6 mil tax levy	1,151,114	—
Bond retirement 1.7 mil tax levy	34,569	1,113,833
Total	<u>\$ 1,192,170</u>	<u>\$ 1,119,979</u>

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

6. Property and Equipment

Costs of capital assets related to depreciable lives for June 30, 2008 are summarized below:

	2007	Additions	Transfers	Retirements	2008	Depreciable Life – Years
Land and land improvements	\$ 934,363	\$ 286,116	\$ 212,076	\$ (21,288)	\$ 1,411,267	5 – 25
Building	14,991,221	105,944	1,308,733	(46,975)	16,358,923	10 – 40
Equipment	6,431,973	256,680	522,478	(129,840)	7,081,291	3 – 20
Construction-in-progress	1,253,924	9,834,517	(2,043,287)	–	9,045,154	
Total	23,611,481	10,483,257	–	(198,103)	33,896,635	
Less accumulated depreciation:						
Land and land improvements	312,593	26,364	–	(21,288)	317,669	
Building	6,133,760	561,059	–	(46,975)	6,647,844	
Equipment	4,660,586	544,705	–	(129,840)	5,075,451	
Total	11,106,939	1,132,128	–	(198,103)	12,040,964	
Net carrying amount	\$ 12,504,542	\$ 9,351,129	\$ –	\$ –	\$ 21,855,671	

Construction-in-progress at June 30, 2008, is composed mainly of costs associated with the construction of a Rural Health Clinic building and \$228,166 of capitalized interest.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

6. Property and Equipment (continued)

Costs of capital assets related to depreciable lives for June 30, 2007 are summarized below:

	2006	Additions	Transfers	Retirements	2007	Depreciable Life – Years
Land and land improvements	\$ 934,363	\$ –	\$ –	\$ –	\$ 934,363	5 – 25
Building	14,951,612	–	39,609	–	14,991,221	15 – 40
Equipment	6,055,543	366,812	9,618	–	6,431,973	3 – 20
Construction-in-progress	124,026	1,179,125	(49,227)	–	1,253,924	
Total	22,065,544	1,545,937	–	–	23,611,481	
Less accumulated depreciation:						
Land and land improvements	284,792	27,801	–	–	312,593	
Building	5,590,671	543,089	–	–	6,133,760	
Equipment	4,076,824	583,762	–	–	4,660,586	
Total	9,952,287	1,154,652	–	–	11,106,939	
Net carrying amount	\$ 12,113,257	\$ 391,285	\$ –	\$ –	\$ 12,504,542	

Construction-in-progress at June 30, 2007, is composed mainly of costs associated with the development of a dialysis center.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

7. Long-Term Debt

Long-term liability activity for the year ended June 30, 2008 was as follows:

	June 30 2007	Current Year Additions	Current Year Reductions	June 30 2008	Amounts Due Within One Year
Series 2008 Bonds	\$ —	\$ 8,400,000	\$ (500,000)	\$ 7,900,000	\$ 715,000
Level Acres Mortgage #1	—	31,688	(6,062)	25,626	12,765
Level Acres Mortgage #2	—	82,383	(5,970)	76,413	12,787
	<u>\$ —</u>	<u>\$ 8,514,071</u>	<u>\$ (512,032)</u>	<u>\$ 8,002,039</u>	<u>\$ 740,552</u>

Long-term liability activity for the year ended June 30, 2007 was as follows:

	June 30 2006	Current Year Additions	Current Year Reductions	June 30 2007	Amounts Due Within One Year
Series 1998 Bonds	\$ 750,000	\$ —	\$ (750,000)	\$ —	\$ —

The Kalkaska County Hospital Authority & Subsidiary, Series 1998 unlimited tax general obligation bonds were payable solely from a \$1.7 mil tax levy and the net revenue of the Hospital. The bonds matured April 1, 2007, and bore interest at 4.85%.

The Hospital issued \$8.4 million in unlimited tax general obligation bonds in December 2007. The bonds have interest rates ranging from 5.125% to 5.375% and are payable annually in amounts ranging from \$715,000 to \$1,065,000. The Hospital also intends to issue \$7 million in revenue bonds in September 2008. The proceeds from the 1.6 mil tax levy will be used to retire the unlimited tax general obligation bonds.

Minimum principal payments on long-term debt to maturity as of June 30, 2008, are as follows:

2009	\$ 740,552
2010	776,539
2011	799,630
2012	840,648
2013 and after	4,844,670
Net long-term debt	<u>\$ 8,002,039</u>

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

8. Retirement Plan

The Hospital maintains the Kalkaska Memorial Health Center Retirement Plan, a Section 401(k) plan covering employees having worked more than 1,000 hours per year for two consecutive years. Under the terms of the plan, the Hospital will contribute 1% of employees' compensation and will match employee contributions on a sliding scale up to 4% of employee earnings. Total retirement expense was \$299,824 and \$291,660 for the years ended June 30, 2008 and 2007, respectively.

9. Risk Management

The Hospital is exposed to various risks of loss related to property loss, errors and omissions, employee injuries (workers' compensation), and professional liability claims, as well as medical benefits provided to employees. The Hospital has purchased commercial insurance for the above claims. Settled claims relating to commercial insurance have not exceeded the amount of insurance in any of the past three years.

The Hospital is insured against medical malpractice claims under a claims-based policy, whereby only the claims reported to the insurance carrier during the policy period are covered, regardless of when the incident giving rise to the claim occurred. Under the terms of the policy, the Hospital must pay a deductible toward the costs of litigating or settling any unasserted claims. In addition, the Hospital bears the risk of ultimate costs of any individual claim exceeding the policy limits for claims asserted in the policy year.

Should the claims-made policy not be renewed or replaced with equivalent insurance, claims based on the occurrences during the claims-made term, but reported subsequently, will be uninsured.

The Hospital is not aware of any medical malpractice claims, either asserted or unasserted, that would exceed the policy limits. No claims have been settled during the past three years that have exceeded policy coverage limits. The cost of this insurance policy represents the Hospital's cost for such claims for the year, and it has been charged to operations as a current expense.

Kalkaska County Hospital Authority & Subsidiary

Notes to Consolidated Financial Statements (continued)

10. Administrative, Laundry, and Laboratory Service Agreements

The Hospital has entered into agreements with Munson Medical Center and Subsidiary and Munson Healthcare and Subsidiaries to receive administrative services including an administrator, accounting services, physical therapy, certain laboratory tests, and other miscellaneous services. Charges for these services to the Hospital amounted to \$1,846,811 and \$1,597,742 for the years ended June 30, 2008 and 2007, respectively, of which \$297,440 and \$308,166, respectively, is included in accounts payable.

Other Financial Information

Kalkaska County Hospital Authority & Subsidiary

Details of Combining Statements of Revenues, Expenses, and Changes in Net Assets

	Year Ended June 30, 2008			
	Kalkaska Memorial Health Center	Dialysis Center	Level Acres	Combined
Operating revenue				
Net patient service revenue	\$ 20,243,825	\$ 205,190	\$ —	\$ 20,449,015
Other	909,663	15,369	97,027	1,022,059
Total operating revenue	21,153,488	220,559	97,027	21,471,074
Operating expenses				
Salaries and wages	8,303,096	169,725	—	8,472,821
Employee benefits and payroll taxes	2,695,816	54,312	—	2,750,128
Medical supplies and drugs	2,323,241	127,899	3,485	2,454,625
Professional services and consultant fees	523,512	—	—	523,512
Purchased services	2,469,781	72,890	36,520	2,579,191
Insurance	257,742	2,831	—	260,573
Occupancy	585,099	22,614	33,328	641,041
Equipment, software, and maintenance	356,250	1,298	865	358,413
Depreciation	1,093,217	24,185	14,726	1,132,128
Other	1,059,714	6,917	3,310	1,069,941
Total operating expenses	19,667,468	482,671	92,234	20,242,373
Operating income	1,486,020	(262,112)	4,793	1,228,701
Other income (expense)				
Investment income	212,158	—	—	212,158
Contributions	59,610	—	—	59,610
Interest on debt related to capital assets	—	—	(4,327)	(4,327)
Tax levy revenue	1,192,170	—	—	1,192,170
Total other income	1,463,938	—	(4,327)	1,459,611
Increase in net assets	2,949,958	(262,112)	466	2,688,312